Note:

It is important to note that the Treasury Strategy Statement is adopted by the Council, based upon advice from its external treasury advisors, and accordingly the Strategy is tailored to meet the specific and unique needs of the Council. All financial information contained within this Report and Statement should not be used by any individual or organisation as a basis for making investment or borrowing decisions. The Council and its treasury advisors will not accept any liability on behalf of any individual or organisation that seeks to act on the financial information contained within this Report and Statement.

Meeting of the Council – 28th February, 2022

Report of the Audit and Standards Committee

Treasury Management

Purpose

1. The purpose of this report is:

- To outline treasury activity in the year 2021/22 up to the end of December 2021.
- To seek approval of the Treasury Strategy Statement 2022/23.

Recommendations

2. It is recommended:

- That the treasury activities in 2021/22, as outlined in this report, be noted.
- That the Treasury Strategy 2022/23, attached as Appendix 2, be approved.
- That the Director of Finance and Legal be authorised to affect such borrowings, repayments and investments as are appropriate and consistent with the approved Treasury Strategy and relevant guidance.

Background

3. Treasury Management entails the management of the Council's cash flows, its borrowings and investments, the management of the associated risks and the pursuit of the optimum performance or return consistent with those risks.

4. The Council undertakes treasury management activity on its own behalf and as administering authority for the West Midlands Debt Administration Fund (WMDAF). We are responsible for administering capital funding of £731m on our own account and another £94m on behalf of other West Midlands councils in respect of the WMDAF. The treasury function is governed by the Council's Treasury Policy Statement and Treasury Management Practices.

5. Our borrowing and investment activities in the current year have been undertaken in the context of historically low interest rates. The Bank Base Rate was increased from its historic low of 0.10% to 0.25% in December 2021 in response to inflationary pressures.

6. Appendix 2 contains some detailed economic commentary but in summary the Monetary Policy Committee is expected to increase interest rates very slowly to counter what are anticipated to be temporary inflationary pressures that are expected to peak in 2022 before inflation returns to its long-term norm. Any pressure to increase rates is tempered by the effect that the Omicron variant of the Coronavirus will have on economic activity in the near term.

7. CIPFA released the new edition of the Treasury Management Code and Prudential Code in December 2021. Due to the timing of the release, local authorities do not have to comply with the reporting requirements of the codes until 2023/24. The main changes relate to further restrictions and reporting requirements for commercial investments.

8. In November 2020 HM Treasury prohibited access to Public Works Loans Board loans for the purpose of funding investments purely for commercial income, and the revised code prohibits local authorities any new commercial investments altogether with immediate effect. Furthermore, it advises that authorities review options for exiting from commercial investments and summarise the review in their annual treasury management strategies, but there is no compulsion to sell existing investments. The revised code requirements on commercial investments do not impact on Dudley MBC as we already have a long-standing policy to refrain from investing in assets purely for revenue income or other financial return (see Section 7 of the Treasury Management Strategy).

Treasury Activity 2021/22 - Dudley Fund

9. Treasury activities in the current year have been undertaken in the context of the Treasury Strategy Statement 2021/22 approved by Audit Committee and Full Council in February 2021. In that document we anticipated that long term borrowing would be required in the next 12 months due to cashflow need.

10. Our investments up to December 2021 have averaged £49.8m (with significant day to day variation as a result of cash flow). The average return on these investments was 0.07%. All investments were placed with institutions that satisfied the criteria for credit-worthiness set out in the Treasury Strategy Statement 2021/22. The performance of our investments is largely dependent on movements in short-term (up to one year) rates. The average 7-day LIBID[1] rate for the year to date has been -0.08%. Cash balances have been lower than at the same time last year but still relatively high due to the on-going effect of Covid-related grants paid in advance by Central Government, some of which are due to be repaid in the near term. Our investment activity for 2021/22 (to date) is set out in more detail in Appendix 1. This includes investments carried forward from 2020/21.

11. The returns outlined above have been achieved without compromising on the security of the Council's investments. We have maintained and continue to maintain an approved investment list that sets the highest rating standards. We have an account with the Government's Debt Management Office (DMO) which provides maximum security but relatively low returns. We use this account extensively due the fact that we have strict credit criteria in our Investment Strategy for non-government counterparties.

12. The average value of long-term borrowings up to the end of December 2021 was £613.3 million. The average rate of interest on these borrowings was 3.62% and they were due to mature on dates ranging from the current year to 2061. To date no new loans have been taken out in 2021/22.

13. We are monitoring cash flows and interest rates closely and anticipate that, due to the Council's capital programme, planned use of reserves and loan maturities, further borrowing may be taken in the second half of 2021/22.

Treasury activity 2021/22 - WMDAF

14. The Council has taken 6 short term loans in the year to date to manage daily cash flow for the WMDAF. The average value of the borrowing has been £2.9m at an average rate of 0.04% for an average duration of 149 days. The latest estimate of interest payable by members of the WMDAF in 2021/22 is 5.4%.

Treasury Strategy Statement 2022/23

15. The Treasury Strategy Statement covers our latest capital funding requirements, our view of interest rate movements and our strategy for borrowing and investment in the light of that view. As such, it needs to be reviewed annually. The proposed Treasury Strategy Statement for 2022/23 is attached as Appendix 2.

16. Our expectations for interest rates advised by our treasury advisors Link Group, which will be subject to continuous review with our treasury advisors, are as follows:

- **Short-term rates**. The Bank Rate will remain at 0.25% until March 2022 and rise to 0.75% by March 2023.
- **Medium-term rates**. 5-year PWLB certainty rate is expected to be 1.50% in March 2022 and rise to 1.70% by March 2023.
- **Long- term rates**. 50-year PWLB certainty rate is expected to be 1.70% in March 2022 and rise to 2.00% by March 2023.

17. The Local Government Act 2003 introduced a system of "prudential borrowing" allowing councils to set their own borrowing limits subject to criteria of prudence and affordability. These criteria are set out in more detail in the Chartered Institute of Public Finance & Accountancy (CIPFA) Prudential Code which specifically requires us to set a number of prudential indicators. The proposed indicators that relate to treasury management are set out in the Treasury Strategy Statement.

18. In order to protect the Council's position if an individual or organisation were to act upon the views expressed in this report, we have deemed it necessary to produce a disclaimer which is shown as a note at the head of the report and Appendix 2.

<u>Finance</u>

19. Forecasts of performance against budget for treasury management activities are sensitive to movements in cash flow and interest rates.

<u>Law</u>

20. The Council has adopted CIPFA's Treasury Management in the Public Services: Code of Practice 2017 which requires the Council to approve a treasury management strategy before the start of the financial year and provide a mid-year update on treasury management activity. In addition, the Department for Communities and Local Government (DCLG) issued revised Guidance on Local Authority Investments in 2010 that required the Council to approve an investment strategy before the start of each financial year. This report fulfils the legal obligation under the Local Government 2003 to have regard to both the CIPFA code and the DCLG guidance.

<u>Risk Management</u>

21. Treasury Management, by its nature entails the management of financial risks, specifically credit risk for investments which is mitigated by limiting acceptable counterparties to those of the highest credit quality and imposing counterparty limits for non-government institutions; and interest rate risk which is mitigated by prudential indicators detailed in Appendix 2.

Equality Impact

22. The treasury management activities considered in this report have no direct impact on issues of equality.

Human Resources/Organisational Development

23. There are no Human Resources/Organisational Development implications associated with this report.

Commercial/Procurement

24. The over-riding purpose of the Council's Treasury Strategy is day to day cash management and not income generation. The strategy prioritises security and liquidity of cash investments over yield. Once those are met, we aim to secure the maximum yield from our investments held with the small number of counterparties that meet the strict criteria laid out in our Annual Investment Strategy.

Council Priorities

25. Treasury Management supports the Council's capital investment priorities as set out in the approved Capital Strategy.

…..……………..…………………………………….

Chair of the Audit and Standards Committee

Appendix 1

Investment Activity 2021/22 to 5th January 2022

Counterparties	Number of investments	Average value £ million	Average rate %	Average duration (days)
Debt Management Office	70	9.67	0.01	11
Other Local Authorities *	5	4.08	0.12	100
Bank of Scotland Call Account	n/a	0.04	0.00	Call
Santander Call Account	n/a	6.95	0.03	Call
Santander Notice Account	n/a	5.88	0.25	35 day notice
HSBC Call Account	n/a	8.15	0.01	Call
HSBC Notice Account	n/a	6.29	0.18	30 day notice
Barclays Call Account	n/a	8.72	0.01	Call

*Includes investments carried forward from 2020/21

Note:
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DUDLEY METROPOLITAN BOROUGH COUNCIL
TREASURY STRATEGY STATEMENT 2022/23

1.0 Introduction

1.1 This Treasury Strategy Statement details the expected activities of the treasury function in the financial year 2022/23. The suggested strategy is based upon officers' views of interest rates as advised by external advisors, supplemented with leading market forecasts. It should be noted that the use of expert external advisors does not remove the responsibility of members and officers for treasury management functions and that those functions cannot be delegated to any outside organisation. The strategy covers:

- the current portfolio position
- prudential and treasury indicators
- prospects for interest rates
- temporary investment strategy
- requirements and strategy for long-term borrowing
- debt rescheduling and premature repayment opportunities
- treasury implications for the Housing Revenue Account (HRA)

2.0 Current Portfolio Position

2.1 The Council's estimated debt position as at 1st April 2022 is as follows:

	£m
Long-term debt:	
- PWLB fixed rate	517.3
- PWLB variable rate	0.0
- Market fixed rate	71.5
- Market LOBO*	10.0
Short-term debt	0
Total debt	598.8

*Lenders Option Borrowers Option (LOBO). This loan was at a fixed rate of 4.6% until February 2009 after which the rate may be varied at the lender's option. If the lender exercises this option to vary the rate then we, as the borrower, have the option to repay the loan.

2.2 The average rate of interest on the above debt is expected to be 3.73%.

2.3 The average level of investments held by the Council during 2021/22 to December 2021 was £49.8m. Cashflow monitoring indicates that long term borrowing may be required in the next 12 months.

2.4 The Council also administers the debt of the former West Midlands County Council on behalf of the West Midlands districts. The estimated debt position at 1st April 2022 is as follows:

	£m
Long-term debt:	
- PWLB fixed rate	72.6
- Market LOBO	10.0
Short-term debt	4.0
Total debt	**86.6**

2.5 The average rate of interest charged to the West Midlands fund is expected to be 5.24%.

3.0 Prudential & Treasury Indicators

3.1 Under the Local Government Act 2003 and the Prudential Code for Capital Finance in Local Authorities, local authority capital spending and its borrowing to fund that spending is limited by what is affordable, prudent and sustainable. The Prudential Code sets out a number of indicators that enable the authority to assess affordability and prudence. The following indicators are relevant for the purposes of setting an integrated treasury management strategy.

3.2 Treasury Indicators in the Prudential Code

The Prudential Code requires that the total external debt does not exceed the Authorised Limit for external debt and only exceeds the Operational Boundary for external debt temporarily on occasions due to variation in cash flow.

These external debt indicators are intended to ensure that levels of external borrowing are affordable, prudent and sustainable. The authorised limit for external debt is a statutory limit (section 3 of the Local Government Act 2003) that should not be breached under any circumstances. It has been calculated to take account of the Council's capital expenditure and financing plans and allowing for the possibility of unusual cash movements. The operational boundary for external debt has also been calculated with regard to the Council's capital expenditure and financing plans allowing for the most likely, prudent, but not worst-case scenario for cash flow. Temporary breaches of the operational boundary, due to variations in cash flow, will not be regarded as significant. Actual external debt represents the closing balance for borrowing and other long-term liabilities.

	2020/21 £m	2021/22 Revised £m	2022/23 Revised £m	2023/24 Revised £m	2024/25 Revised £m
Authorised limit for external debt : Borrowing	n/a	876	933	922	931
Other long term liabilities	n/a	15	12	12	11
Total	n/a	891	945	934	942
Operational boundary *: Borrowing	n/a	805	818	830	865
other long term liabilities	n/a	15	12	12	11
Total	n/a	820	830	842	876
Actual External Debt: Borrowing	766.6	n/a	n/a	n/a	n/a
Other long term liabilities	17.0	n/a	n/a	n/a	n/a
Total	**783.6**	n/a	n/a	n/a	n/a

3.3 Gross Debt and the Capital Financing Requirement

This is a key indicator of prudence. In order to ensure that over the medium-term debt will only be for a capital purpose, the local authority should ensure that debt does not, except in the short term, exceed the total of capital financing requirement in the preceding year plus the estimates of any additional capital financing requirement for the current and next two financial years.

The Council has met this requirement in 2021/22 and expects to do so in future years. This view takes into account current commitments, existing plans and the proposals in the approved budget.

3.4 Interest rate exposures

These indicators allow the Council to manage the extent to which it is exposed to changes in interest rates. The upper limit for fixed interest reflects the fact that it is possible to construct a prudent treasury strategy on the basis of using only fixed rate debt and investments, so long as the maturity dates of these debts and investments are reasonably spread. The same does not apply to variable rates where a 100% exposure could lead to significant year on year fluctuations in the cost of debt. The upper limit for variable rate exposure allows for the use of variable rate debt to offset our exposure to changes in short-term rates on our portfolio of investments. This limit reduces over time as our strategy is to gradually reduce our level of investments.

	2021/22	2022/23	2023/24	2024/25
Upper limit for fixed interest rate exposure	100	100	100	100
Upper limit for variable rate exposure	10	10	10	10

3.5 Maturity structure of borrowing and investments

The maturity structure of fixed rate borrowing is designed to protect against excessive exposures to interest rate changes in any one period, in particular over the course of the next ten years.

Dudley MBC Maturity Indicator	Upper Limit %	Lower Limit %
Under 12 months	15	0
12 months and within 24 months	15	0
24 months and within 5 years	20	0
5 years and within 10 years	25	0
10 years and above	100	50

West Midlands Debt Administration Fund Loan Maturity Indicator *	Upper Limit %	Lower Limit %
Under 12 months	26	0
12 months and within 24 months	20	0
24 months and within 5 years	54	0

* The WMADF will close in March 2026 no new long term loans will be required. The above indicator is based on the maturity of the remaining loans in the fund.

3.6 Upper Limit for total principal sums invested over 364 days

The purpose of the limits for principal sums invested for periods longer than 364 days is to contain the Council's exposure to the possibility of loss that might arise as a result of having to seek early repayment of principal sums invested. On the basis of prudent treasury management the proposed upper limit on principal maturing in any one year for sums invested for over 364 days is £10m.

4.0 Economic Background

4.1 The Monetary Policy Committee (MPC) voted 8-1 to raise Bank Rate by 0.15% from 0.10% to 0.25% and unanimously decided to make no changes to its programme of quantitative easing purchases due to finish in December 2021 at a total of £895bn. The MPC had disappointed financial markets by not raising Bank Rate at its November meeting. Until Omicron burst on the scene, most forecasters, therefore, viewed a Bank Rate increase as being near certain at this December meeting due to the way that inflationary pressures have been comprehensively building in both producer and consumer prices, and in wage rates. However, at the November meeting, the MPC decided it wanted to have assurance that the labour market would get over the end of the furlough scheme on 30th September without unemployment increasing sharply; their decision was, therefore, to wait until statistics were available to show how the economy had fared at this time.

4.2 On 15th December we had the CPI inflation figure for November which spiked up further from 4.2% to 5.1%, confirming again how inflationary pressures have been building sharply. However, Omicron also caused a sharp fall in world oil and other commodity prices; (gas and electricity inflation has generally accounted on average for about 60% of the increase in inflation in advanced western economies). Other elements of inflation are also transitory e.g. prices of goods being forced up by supply shortages, and shortages of shipping containers due to ports being clogged have caused huge increases in shipping costs. But these issues are likely to clear during 2022, and then prices will subside back to more normal levels. Gas prices and electricity prices will also fall back once winter is passed and demand for these falls away.

4.3 Although it is possible that the Government could step in with some fiscal support for the economy, the huge cost of such support to date is likely to pose a barrier to incurring further major expenditure unless it was very limited and targeted on narrow sectors like hospitality. The Government may well, therefore, effectively leave it to the MPC, and to monetary policy, to support economic growth – but at a time when the threat posed by rising inflation is near to peaking.

4.4 This is the adverse set of factors against which the MPC had to decide on Bank Rate. For the second month in a row, the MPC blind-sided financial markets, this time with a surprise increase in Bank Rate from 0.10% to 0.25%. What's more, the hawkish tone of comments indicated that the MPC is now concerned that inflationary pressures are indeed building and need concerted action by the MPC to counter. This indicates that there will be more increases to come with financial markets predicting 1% by the end of 2022. The 8-1 vote to raise the rate shows that there is firm agreement that inflation now poses a threat, especially after the

CPI figure hit a 10-year high this week. The MPC commented that “there has been significant upside news” and that “there were some signs of greater persistence in domestic costs and price pressures”.

4.5 On the other hand, it did also comment that “the Omicron variant is likely to weigh on near-term activity”. But it stressed that at the November meeting it had said it would raise rates if the economy evolved as it expected and that now “these conditions had been met”. It also appeared more worried about the possible boost to inflation form Omicron itself. It said that “the current position of the global and UK economies was materially different compared with prior to the onset of the pandemic, including elevated levels of consumer price inflation”. It also noted the possibility that renewed social distancing would boost demand for goods again, (as demand for services would fall), meaning “global price pressures might persist for longer”.

4.6 On top of that, there were no references this month to inflation being expected to be below the 2% target in two years’ time, which at November’s meeting the MPC referenced to suggest the markets had gone too far in expecting interest rates to rise to over 1.00% by the end of the year. These comments indicate that there has been a material reappraisal by the MPC of the inflationary pressures since their last meeting and the Bank also increased its forecast for inflation to peak at 6% next April, rather than at 5% as of a month ago. However, as the Bank retained its guidance that only a “modest tightening**”** in policy will be required, it cannot be thinking that it will need to increase interest rates that much more. A typical policy tightening cycle has usually involved rates rising by 0.25% four times in a year. “Modest” seems slower than that. As such, the Bank could be thinking about raising interest rates two or three times next year to 0.75% or 1.00%. In as much as a considerable part of the inflationary pressures at the current time are indeed transitory, and will naturally subside, and since economic growth is likely to be weak over the next few months, this would appear to indicate that this tightening cycle is likely to be comparatively short.

4.7 As for the timing of the next increase in Bank Rate, the MPC dropped the comment from November’s statement that Bank Rate would be raised “in the coming months”. That may imply another rise is unlikely at the next meeting in February and that May is more likely. However, much could depend on how adversely, or not, the economy is affected by Omicron in the run up to the next meeting on 3rd February. Once 0.50% is reached, the Bank would act to start shrinking its stock of QE, (gilts purchased by the Bank would not be replaced when they mature).

5.0 Prospects for Interest Rates

5.1 The Council’s Treasury Advisor, Link Asset Services, has provided the following forecast :

	March 2022	March 2023	March 2024	March 2025
Bank Rate	0.25%	0.75%	1.00%	1.25%

5yr PWLB rate	1.50%	1.70%	1.90%	2.00%
10yr PWLB rate	1.70%	1.90%	2.10%	2.30%
25yr PWLB rate	1.90%	2.20%	2.30%	2.50%
50yr PWLB rate	1.70%	2.00%	2.10%	2.30%

5.2 In December the Bank of England became the first major western central bank to put up interest rates in this upswing in the current business cycle in western economies as recovery progresses from the Covid recession of 2020. The next increase in Bank Rate could be in February or May, dependent on how severe an impact there is from Omicron. If there are lockdowns in January, this could pose a barrier for the MPC to putting Bank Rate up again as early as 3rd February. With inflation expected to peak at around 6% in April, the MPC may want to be seen to be active in taking action to counter inflation on 5th May, the release date for its Quarterly Monetary Policy Report. The December 2021 MPC meeting was more concerned with combating inflation over the medium term than supporting economic growth in the short term. Bank Rate increases beyond May are difficult to forecast as inflation is likely to drop sharply in the second half of 2022.

5.3 However, the MPC will want to normalise Bank Rate over the next three years so that it has its main monetary policy tool ready to use in time for the next down-turn; all rates under 2% are providing stimulus to economic growth. We have put year end 0.25% increases into Q1 of each financial year from 2023 to recognise this upward bias in Bank Rate - but the actual timing in each year is difficult to predict. Covid remains a major potential downside threat in all three years as we are likely to get further mutations. How quickly can science come up with a mutation proof vaccine, or other treatment, – and for them to be widely administered around the world? Purchases of gilts under QE ended in December. Note that when Bank Rate reaches 0.50%, the MPC has said it will start running down its stock of QE.

5.4 Our overall strategy will be based on the projections above. However, we will maintain flexibility to take account of unexpected variations from our forecast.

6.0 Annual Investment Strategy

6.1 Our investment activities are subject to government guidance issued under Section 15(1) (a) of the Local Government Act 2003. This section of the Treasury Strategy Statement constitutes an "Annual Investment Strategy" produced in accordance with the guidance.

6.2 The Council holds invested funds, representing income received in advance of expenditure plus balances and reserves held. We have a policy of keeping cash balances at minimum levels by maximising the use of internal borrowing to finance capital expenditure.

6.3 Both the CIPFA Code and the Department for Communities and Local Government (DCLG) require the Council to invests its funds prudently, and to have regard to the security and liquidity of its investments before seeking the highest rate of return or yield. The Council's primary objective in relation to the investment of public funds remains the security of capital. The liquidity or accessibility of the Council’s investments followed by the yields earned on investments is important but are secondary considerations.

6.4 Strategy for “specified investments”

6.4.1 The Council will make use of specified investments (as defined within the terms of the government guidance). These are investments that satisfy the following conditions:

a) The investment is denominated in sterling and any payments or repayments in respect of the investment are payable only in sterling.
b) The Council may require that the investment be repaid or redeemed within 12 months of the date on which the investment was made.
c) The making of the investment is not defined as capital expenditure by legislation.
d) The investment satisfies either of the following conditions:

    I. The investment is made with the UK government, a local authority, a parish council or a community council, or
    II. The investment is made with a body or in an investment scheme of high credit quality.

6.4.2 The Council will be prepared to lend to the West Midlands Combined Authority. Such lending will be as part of arrangements agreed with the Combined Authority and other constituent authorities.

6.4.3 For the purpose of this strategy a body or investment scheme is deemed to be of high credit quality if it has minimum short-term ratings of F1 (Fitch), P1 (Moody’s), and A1 (Standard and Poors).

6.4.4 The Council will also limit risks by applying lending limits and criteria for “high credit quality” as shown below:

Specified Investments Counterparty	**Minimum Short-term Credit Rating***	**Maximum Investment per Counterparty**	**Time Limit**
UK Banks	F1+/P1/A1+	£20m	3 months
	F1/P1/A1	£15m	1 month
UK Local Authorities	n/a	£20m	12 months
UK Government	n/a	none	none

*Fitch/ Moodys /S&P rating agencies respectively. Institutions must have the requisite rating at 2 of the 3 agencies.

6.4.5 Since the financial crisis of 2008, the Council has not allowed investments in non-UK institutions. The existing strategy is based on the implicit assumption that the UK Government would support a failing UK bank. This factor is less relevant in light of the Financial Services (Banking Reform) Act 2013 and proposed regulations. That said, current cash flow predictions do not suggest that there is any compelling need to widen the investment strategy to non-UK institutions and so there is no proposal to change.

6.4.6 The Council understands that credit ratings are good, but not perfect, predictors of investment default. Full regard will therefore be given to other available information on the credit quality of the organisations in which it invests, including credit default swap prices, financial statements, information on potential government support and reports in the quality financial press. No investments will be made with an organisation if there are substantive doubts about its credit quality, even though it may meet the credit rating criteria.

6.4.7 When deteriorating financial market conditions affect the creditworthiness of all organisations, this is not generally reflected in credit ratings, but can be seen in other market measures. In these circumstances, the Authority will restrict its investments to those organisations of higher credit quality and reduce the maximum duration of its investments to maintain the required level of security. The extent of these restrictions will be in line with prevailing financial market conditions. If these restrictions mean that insufficient commercial organisations of high credit quality are available to invest the Authority's cash balances, then the surplus will be deposited with the UK Government, via the Debt Management Office for example, or with other local authorities. This will cause a reduction in the level of investment income earned, but will protect the principal sum invested.

6.4.8 The only indicators with prescriptive values remain to be credit ratings. Other indicators of creditworthiness are considered in relative rather than absolute terms.

6.4.9 If conditions in the financial markets worsen during 2022/23 or other factors indicate that increased security of Council funds is required, the Director of Finance and Legal Services may impose tighter restrictions on the type of investments and institutions used by the Council, than those detailed in this strategy.

6.4.10 The Council banks with HSBC. At the current time, it does meet the minimum credit criteria and has the highest credit rating for a UK bank. Even if the credit rating falls below the Council's minimum criteria HSBC will continue to be used for short term liquidity requirements (overnight and weekend investments) and business continuity arrangements.

6.5 *Strategy for "non-specified investments"*

6.5.1 Non-specified investments are those that do not meet the criteria for a specified investment detailed in 6.4.1 above. The Council does not intend to make any investments denominated in foreign currencies, or any that are defined as capital expenditure by legislation such as company shares. Neither is there an intention to make new long term investments, especially in the light of maximising the length of any non-government investment to 3 months irrespective of its credit quality. Therefore the Council will not place its funds with non-specified investments.

6.6 *Liquidity of investments*

6.6.1 In determining the maximum period for which investments may be held, we will have regard to our most recent cash-flow forecast. We will not enter into an investment where our cash-flow forecast indicates that, as a result of that investment, we would be forced to borrow money at a later date that we would not otherwise have had to borrow.

7.0 Policy on Non-Financial Investments

7.1 Investment in non-financial assets including property is not part of the Council's Treasury Management Strategy**.** The Council will incur capital expenditure on acquisition or development of property only where the primary purpose is regeneration and/or service delivery, and then only where a development would not happen without Council involvement, and the potential regeneration gain justifies any financial or other risks. It will not invest in property for the sole or primary purpose of revenue income or other financial return.

7.2 The Council will not make any investments in fossil fuel companies.

8.0 Policy on the Use of Financial Derivatives

8.1 A financial derivative is a contract whose value is based on, or "derived" from, an underlying financial instrument such as a loan. Local authorities have previously been able to make use of financial derivatives embedded into loans and investments, both to reduce interest rate risk (e.g. forward deals) and to reduce costs or increase income at the expense of greater risk (e.g. LOBO loans).

8.2 The general power of competence in Section 1 of the Localism Act 2011 removes much of the uncertainty over local authorities' use of standalone financial derivatives (i.e. those that are not embedded into a loan or investment). The CIPFA Code requires authorities to clearly detail their policy on the use of derivatives in the annual strategy.

8.3 The Council does not intend to use standalone financial derivatives (such as swaps, forwards, futures and options). Should this position change, the Council may seek to develop a detailed and robust risk management framework governing the use of derivatives, but no change in strategy will be made without full Council approval.

9.0 Requirements and Strategy for Long-Term Borrowing

9.1 The primary factor in determining whether we undertake new long-term borrowing will be cash flow need. We will seek to minimise the time between borrowing and anticipated cash flow need, subject to the need to maintain day to day liquidity.

9.2 The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR), while usable reserves and working capital are the underlying resources available for investment. The Council's strategy is to maintain borrowing and investments at a minimum (well below their underlying levels) thereby maximising the use of internal borrowing. This keeps borrowing costs lower than they would otherwise be and keeping cash balances low reduces credit risk.

9.3 The balance sheet forecast indicates a requirement to increase the level of external borrowing in the medium and long term. Our interest rate expectations (outlined in 5.1) provide a variety of options on the type of borrowing we will undertake:

- That short-term variable rates will be good value compared to long-term rates and are likely to remain so for potentially at least the next couple of years. Best value will therefore be achieved by borrowing short term at variable rates in order to minimise borrowing costs in the short term.

- That the risks intrinsic in the shorter term variable rates are such, when compared to historically relatively low long term fixed funding, which may be achievable in 2022/23, that the Council will maintain a stable, longer term portfolio by drawing longer term fixed rate funding at a marginally higher rate than short term rates.

9.4 Against this background caution will be adopted with the 2022/23 treasury operations. The Director of Finance and Legal Services will monitor the interest rate market and adopt a pragmatic approach to changing circumstances.

Sensitivity of the forecast - The main sensitivities of the forecast are likely to be the two scenarios below. In conjunction with the treasury advisers, we will continually monitor both the prevailing interest rates and the market forecasts, adopting the following responses to a change of sentiment:

- If it were felt that there was a significant risk of a sharp rise in long and short term rates, perhaps arising from a greater than expected increase in world economic activity, then the portfolio position will be re-appraised with the likely action that fixed rate funding will be drawn whilst interest rates are still relatively cheap

- If it were felt that there was a significant risk of a sharp fall in long and short term rates, due to growth rates remaining low or weakening, then long term borrowings will be postponed

9.5 With respect to the West Midlands Debt, variances due to timing differences between the maturity profile of the debt and repayments from authorities can be managed by short term borrowing in 2022/23.

9.6 The approved sources of long-term and short-term borrowing are:

- Public Works Loans Board
- Any institution approved for investments (above)
- Any other bank or building society authorised to operate in the UK
- UK public and private sector pension funds (except the West Midlands Pension Fund)

In addition, capital finance may be raised by finance leases and similar arrangements which may be classed as debt liabilities.

10.0 Debt Rescheduling and Premature Repayment Opportunities

10.1 We may consider rescheduling or premature repayment with the following aims:

- the generation of cash savings at minimum risk
- in order to help fulfil the strategy outlined in 9 above
- in order to enhance the balance of the long-term portfolio (by amending the maturity profile and/or the balance of volatility).

10.2 Any rescheduling or premature repayment will be reported to an appropriate committee at the meeting following its implementation.

11.0 HRA Self Financing

11.1 On 1st April 2012, the Council notionally split each of its existing long-term loans into General Fund and HRA pools. In the future, new long-term loans borrowed will be assigned in their entirety to one pool or the other. Interest payable and other costs/income arising from long-term loans (e.g. premiums and discounts on early redemption) will be charged/ credited to the respective revenue account.

11.2 Differences between the value of the HRA loans pool and the HRA's underlying need to borrow (adjusted for HRA balance sheet resources available for investment) will result in a notional cash balance which may be positive or negative. An average of this notional balance will be calculated annually and interest transferred between the General Fund and HRA at an internally determined rate of interest, adjusted for risk.

12.0 Training

12.1 CIPFA's Code of Practice requires the Director of Finance and Legal Services to ensure that all members tasked with treasury management responsibilities, including scrutiny of the treasury management function, receive appropriate training relevant to their needs and understand fully their roles and responsibilities. Relevant training is provided by Link Asset Services to the members of the Audit & Standards Committee and other members of the Council.

12.2 The Council recognises the importance of ensuring that all staff involved in the treasury management function are fully equipped to undertake the duties and responsibilities allocated to them. It will therefore seek to appoint individuals who are both capable and experienced and will provide training for staff to enable them to acquire and maintain an appropriate level of expertise, knowledge and skills. The Director of Finance and Legal Services will recommend and implement the necessary arrangements.

13.0 Treasury Management Advisors

13.1 The Council uses Link Asset Services as its external treasury management advisers. The Council recognises that responsibility for treasury management decisions remains with the organisation at all times and will ensure that undue reliance is not placed upon our external service providers.

13.2 It also recognises that there is value in employing external providers of treasury management services in order to acquire access to specialist skills and resources. The Council maintains the quality of the service with its advisors by holding regular meetings and tendering periodically for the provision of treasury management advice.

13.3 The Council receives the following services from Link Asset Services:

a. Credit advice
b. Investment advice
c. Technical advice
d. Economic & interest rate forecasts
e. Workshops and training events for officers and members